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US TRADE REPRESENTATIVE - MICHAEL DELANEY AND VICTORIA KADEL

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TAGS: ECON PGOV MV
SUBJECT: Maldives Budget Reduces Government Deficit

¶1. (SBU) Summary. The Government of the Maldives (GOM) proposed an austere 2010 budget to its Parliament. The budget projects both reduced spending and growing tax collection that would reduce the government budget deficit from 29% of GDP in 2009 to 16% of GDP in 2010 and reaching a mere 3% of GDP in 2011. If the GOM meets these projections they would fulfill the demanding targets of the IMF program. However, the GOM is projecting substantial revenue from taxes in 2010 which have not been approved by Parliament, so these estimates are far from certain. The political opposition, which controls the most seats in Parliament, has severely criticized the proposed budget, although their Speaker told Poloff that he expected that the budget would be approved. End Summary.

¶2. (U) The GOM presented its budget on November 24 in the national language of Dhivehi, and an English translation of Finance Minister Ali Hashim's speech and the GOM proposed budget is not available. Post has based this report on official fiscal data received from the Ministry of Finance, news reports of political opposition to the budget, and Poloff contacts with the opposition. The GOM will publish its final budget in English after the Maldivian Parliament approved the budget. Parliament is currently debating the proposed budget, and the GOM expects a vote on the budget before Christmas.

Ambitious Budget projects Declining Deficits

¶3. (SBU) Maldivian Minister of Finance Hashim argued that the 2010 budget fulfills the GOM small government pledge. Total expenditure would decrease by 7 percent to 48 percent of GDP. Total revenue would increase from 28 percent of GDP in the revised 2009 budget to 33 percent of GDP in 2010. The 2010 budget deficit (excluding grants) is estimated to be $258 million or about 16 percent of GDP. According to the medium term GOM budget framework, the deficit is expected to decline to 3 percent of GDP in 2011 and post a small surplus in 2012.

Government of Maldives - Budget 2009-2010
--In millions of USD--

2009	
Revenue	$414 (28% OF GDP)
Expenditure	$851 (58% OF GDP)
--Current	$617
--Capital	$234
--Net lending	0

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Budget deficit    $430 (29%OF GDP)
Budget deficit
with grants       $382 (26% OF GDP)

2010
Revenue         $531 (33% OF GDP)
Expenditure       $789 (48% OF GDP)
--Current       $648
--Capital         $156
--Net lending     $16
Budget deficit    $258 (16%OF GDP)
Budget deficit
with grants       $234 (15%OF GDP)
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Notes: Expenditure includes interest on government debt but excludes loan repayments. The budget was presented in Ruffiya but we converted it to USD on the official exchange rate of 12.8Rf/$1 USD. These estimates are based on data provided by the Ministry of Finance, Maldives.

¶4. (SBU) The proposed 2010 budget contains optimistic revenue forecasts. Revenue is expected to increase by a whopping 28 percent to 33 percent of GDP in 2010. (Note: according to information supplied by the Finance Ministry, Maldives enjoyed a revenue to GDP ratio of over 30% in the last few years. The ratio increased to over 40% in the post tsunami period of 2005-2008. End Note.) Tax revenue is to increase by 35 percent and will contribute 50 percent of total revenue. The balance will come from resort lease rentals, state owned company dividends, worker permit fees and an assortment of other charges. According to media reports, Minister Hashim

revealed plans to introduce two new taxes in 2010. For the first time, GOM plans to have a corporate income tax (business profits tax) and a goods and services tax in the tourism sector. These two taxes will contribute $51 million, or 10 percent of total revenue in
¶2010. Currently, Maldives tax structure contains import duty, a bank profit tax, a tourism bed tax and licenses and fees. Parliament must approve the two proposed taxes, and the GOM must develop expertise to successfully implement the new taxes. The corporate tax is designed to generate $23 million in 2010. The new tourism tax is to be introduced in the fourth quarter of 2010 and is expected to generate $28 million in 2010 and $125 million in 2011, when it is fully operational. In addition, the budget also contains a new airport tax.

¶5. (SBU) On the expenditure side, total expenditure will decrease by 7 percent due to a drastic cut in capital expenditure. Current expenditures will actually increase. The number of government employees will be reduced in 2010, although the documents did not specify the number of reductions. According to news reports, Minister Hashim said that the GOM has given consideration to recommendations by the IMF, ADB and WB to introduce targeted subsidies and transfer government debt owed to Maldives Monetary Authority (MMA) into bonds.

¶6. (SBU) The GOM expects that the 2010 budget deficit of $258 million will be met by foreign grants and loans, privatization receipts and sale of MMA bonds. The Maldives expects foreign grants of $15 million and (net) foreign loans of approximately $8.5 million to fill the budget gap in 2010. In addition, the GOM expects to receive privatization receipts of $101 million. The GOM anticipates raising $148 million from sales of government bonds.

Strong Political Opposition to the proposed Budget

¶7. (U) The main opposition, Dhivehi Rayyithunge Party (DRP), which holds two more seats in the Parliament than the government (although neither has a majority), has severely criticized the 2010 budget. The DRP says the budget is a "deficit budget" because without approval of new taxes will result in a government deficit of 40% of the proposed expenditure and loan repayments (but not 40% of GDP). Dr Abdulla Mausoom, Secretary General of the DRP, told post that the DRP is concerned about the heavy reliance on two new taxes (corporate tax and tourism tax) since these taxes must be approved

by Parliament. Further, the introduction of these taxes will require a new tax administration law to be passed by the Parliament. He doubts if the legislation could be passed in Parliament in a timely manner and it will be very difficult to set up a tax administration quickly. As a result, DRP expects tax incomes to fall short of the forecast. The DRP also criticizes government privatization plans. Mausoom says that as the government plans to sell profit making companies, it will lose potential revenue sources. For instance, the budget forecasts $42 million from dividends of state companies in 2010, compared with $68 million in ¶2009. He stressed that DRP is not against foreign investment. However, foreign investment should come from new investments and not by selling existing government assets.

¶8. (U) According to Mausoom, the GOM budget is disappointing because it does not meet the government's promises when they were elected. Before coming into power, the governing party was very vocal about people's needs. The proposed 2010 budget has a limited focus on economic activity and it fails to deliver on the GOM development pledges. Despite promises to reduce government staff, Mausoom claims the government will continue to spend on political appointees. Mausoon also complains that the budget does not provide sufficient funds for independent commissions (i.e. Human Rights, Civil Service, Elections, Anti Corruption) important for democracy and tourism promotion as well as for health and education. These activities would receive reduced funding in 2010 under the proposed budget.

¶9. (SBU) Despite public opposition, the DRP may eventually support the budget. The DRP Speaker of the Parliament told Poloff privately that there will be a great deal of grandstanding for political reasons, but he does not anticipate any problems passing the budget. Although the Parliament has made some headway recently, passing two bills, Parliament has only passed four bills this session, and only

one of them - to raise the tourist tax - related to the economic crisis.

¶10. (SBU) Comment. The GOM deserves credit for presenting a 2010 budget that meets the tough IMF budget deficit targets, but the road ahead will be very difficult. Although the DRP Speaker said that they would support the budget, it remains to be seen if they follow through to support the government on austerity budgets and to lay off government employees. Moreover, even if the legislation is passed, it will be very hard to successfully implement these new laws. The GOM has limited experience collecting direct taxes, since they primarily relied on import duties before, and they will need substantial technical assistance to successfully meet their revenue goals. End Comment.

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